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USNATO PLEASE PASS TO AMBASSADOR NULAND  
DEPARTMENT FOR EUR/SCE, EUR/RPM  
DEFENSE FOR OSD/ISP/NATO POLICY

E.O. 12958: N/A

TAGS: [PREL](#) [OREP](#) [PGOV](#) [MARR](#) [HR](#)

SUBJECT: CROATIA SCENE SETTER FOR AMBASSADOR NULAND AND THE  
NATO ROAD SHOW

¶1. SUMMARY: The last few months have brought a string of good news for Croatia and the government of Prime Minister Ivo Sanader. With EU accession negotiations opened on October 4 and fugitive general Ante Gotovina arrested in Spain on December 7, Croatia has now cleared major political obstacles in its path to Euro-Atlantic integration. What remains are the more difficult agendas of defense and economic reform. As a candidate for NATO membership, Croatia continues to make progress in defense reform and demonstrate that it will be a net contributor to the Alliance's new missions. Without traditional U.S. bilateral military assistance due to ASPA restrictions, our bilateral military exchanges focus on improving NATO interoperability for the Croatian Armed Forces (CAF). On the economic front, Croatia has made steady, albeit uneven progress in enacting the reforms necessary for it to keep pace with its more advanced northern neighbors. Our goal is to help quicken the pace of reform and make Croatia a source of stability and economic prosperity in the region. END SUMMARY.

#### THE NEW FACE OF THE NATIONALIST PARTY

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¶2. PM Ivo Sanader's Croatian Democratic Union (HDZ) party was elected in November 2003 on a platform promising to bring Croatia into the EU and NATO. The HDZ has proven it is no longer cut from the same cloth as the nationalist HDZ of the late president Franjo Tudjman in the 1990s. PM Sanader made important gestures immediately after taking office -- visiting the Serb Community on Orthodox Christmas, reaching out to the Muslim minority, and signing coalition agreements with the Serb parliamentary grouping - - which were almost unthinkable just months before. In addition, he has made great strides in normalizing relations with Serbia and Montenegro and Bosnia and Herzegovina, including high-level visits, visa-free travel and free trade agreements.

¶3. The opening of EU accession negotiations on October 4, 2005 was a major victory for the Sanader government. Croatia cleared a further hurdle on December 7, when fugitive general Ante Gotovina was arrested in Spain and transferred to the ICTY in The Hague to stand trial for charges of war crimes committed in the aftermath of Croatia's Operation Storm, which liberated the rebel-Serb-occupied Krajina region in 1995. The Gotovina arrest, applauded by the U.S. and the international community, was not popular domestically, as many Croats consider Gotovina a hero of their war of independence; to its credit,

however, and at some potential political cost, the HDZ worked to keep the few protests which did occur after the arrest focused on "support for Gotovina" rather than venting anger at the international community or the ICTY.

#### EURO-ATLANTIC INTEGRATION: NOT IF, BUT WHEN

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14. With Gotovina in the Hague, the GOC is focused on promoting its goal of NATO membership to the general public. There is a general consensus among the political elite that Croatia belongs in NATO, but the GOC acknowledges that it must generate similar levels of support among the general public, and is implementing its PR strategy.

15. The MOD and General Staff are committed to increasing participation in NATO Peacekeeping Operations, and are planning for and funding operations through 2015. Over the summer, the parliament approved tripling to 150 Croatia's troop (currently primarily Military Police) contribution to NATO's ISAF mission in Afghanistan. A Croatian MP platoon is currently in its seventh rotation in Kabul and the first increase in ISAF contributions will be a seven man Military Liaison and Observation Team to deploy with the Lithuanian PRT in Chagcharan. Currently, Croatia also has 31 persons deployed on 10 UN peace support operations, including Major General Dragutin Repinc, who assumed command on December 29 of the UNMOGIP operation in Kashmir.

16. Croatia has an ambitious military reform program in place to make the armed forces "NATO-ready" by 2007 a difficult task under the best circumstances. The government signed off in mid 2005 on the Strategic Defense Review (SDR), which bases future defense planning on the

assumption that Croatia has no serious threats to its territorial integrity and will be a full partner in collective defense through NATO. The Long Term Development Plan for the Croatian Armed Forces, currently in semi-final draft form, attempts to bridge the gap between the defense reform vision of the SDR and the likely fiscal shortfalls over the next three-five years. Defense spending is currently just short of the Prague Capabilities Commitment level of 2 percent of GDP, although obligatory pension payments to war veterans and a personnel-heavy defense budget leave only minimal resources for much-needed equipment procurement. U.S. firms, including Lockheed-Martin, ITT and Motorola are supplying equipment to the Croatian military and General Dynamics is currently bidding on contracts for the major, upcoming purchase of armored personnel carriers. We support Croatia's NATO ambitions, but have been very clear in our message that defense reform is an essential pre-condition for Croatia to demonstrate that it will become a net contributor to security through NATO operations.

#### MAKING MOST OF MILITARY TO MILITARY ENGAGEMENT

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17. As Croatia has not signed an Article 98 agreement, International Military Education and Training (IMET) and Foreign Military Financing (FMF) programs were suspended in June 2003. Prior to the suspension, the U.S. provided \$4.2 million in IMET grants, which allowed over 350 Croatian civilian and military personnel to attend training in the U.S. and an additionally 300 MOD personnel to receive training from Mobile Education Teams in Croatia. Many of Croatia's IMET graduates now hold key positions of prominence within the Croatian Defense Ministry and Joint Staff. The MoD still considers IMET one of the most important tools for the transition of its armed forces to a modern, NATO-ready force, and is spending some of its limited training funds to send two senior general staff officers to English language training in the U.S. that would otherwise have been IMET supported.

18. Prior to FMF suspension, Croatia used FMF grants

totaling \$18.4 million to purchase equipment for force modernization and NATO interoperability. These purchases included the acquisition of VHF and NTDR digital radios, Night Vision Devices, and MILES training simulations equipment. The Croatian Air Force also used FMF grants to upgrade two Mi-8 helicopters with NATO-compatible radios and identification systems.

¶9. **Bilateral Activities:** The USEUCOM-sponsored Joint Contact Team Program, an essential element of bilateral military engagement, has sponsored over five hundred bilateral familiarization events with the Croatian Armed Forces since 1996. Since the suspension of IMET and FMF, JCTP programs have been increasingly focused on improving the Croatian Armed Forces' NATO interoperability. In FY 05, the JCTP Program conducted twenty-one events that covered a wide array of military activities to help focus the professional development and effective transition of the Croatian Armed Forces.

¶10. Another vital aspect of US engagement has been the Minnesota National Guard's collaboration with the Croatian Armed Forces under the State Partnership Program. Since 1997, the Minnesota National Guard, in conjunction with the USEUCOM JCTP program, has participated in more than 80 bilateral exchanges in a variety of fields to include infantry operations, pilot exchanges, and instruction on the challenges of recruitment. This state partnership continues to grow both in scope and quality. Six state-partnership events were conducted in 2005 culminating in a very successful platoon exchange in July, in which a composite Croatian Platoon deployed to Minnesota and trained alongside the National Guard unit in final preparation for deployment to Iraq. The training included land navigation, light infantry operations, Peace keeping and operations in urban terrain. Reciprocal platoon exchanges are programmed for FY 06 and FY 07, building to a proposed infantry company exchange in FY 08.

¶11. The Marshall Center is also increasingly valued as an engagement tool that allows Croatian MOD personnel, and the Ministries of the Interior and Foreign Affairs to interface with US military officers and regional counterparts in

residency programs and regional conferences. Since 1995, the Marshall Center has hosted 135 Croatian participants in its residency programs in Advanced Security Studies, Terrorism and Security Studies, and the Senior Executive Seminars. Among others, the current Croatian Ambassador to NATO and the head of the Counter Intelligence Agency (POA) are Marshall Center graduates.

THE WAR IS OVER, BUT THE SCARS REMAIN  
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¶12. Among the more important accomplishments of PM Sanader's government are advances in addressing the legacy of the 1991-95 war. In addition to cooperation with the ICTY and sounder adjudication of war crimes, the HDZ government has made significant progress on refugee returns based on its December 2003 coalition agreement with ethnic Serb parliamentarians. International observers such as the OSCE and UNHCR have praised the government's pace of reconstruction of war-damaged housing and return of refugee property, although ethnic discrimination and resistance to change at the local level are persistent challenges.

¶13. Of the estimated 350,000 people, mostly ethnic Serbs, who were displaced during the war, about 134,000 have returned. This leaves approximately 215,000 refugees and internally-displaced persons derived from the 1991-1995 war most of these ethnic Serbs now living in Serbia and Montenegro and Bosnia and Herzegovina. The UNHCR re-registration project of March 2005 clarified the number of true refugees, concluding that the majority have settled in place and do not plan to return. An OSCE/USAID survey indicated that from five to twenty percent of refugees

would return if guaranteed employment and housing.

¶14. As suggested by the OSCE, UNHCR, and the European Commission, the Government has created a "road map" with the goal of closing the refugee file in 2006. Elements of this include specific benchmarks such as the resolution of refugee housing, equal access to information and government services, and information on war crimes indictments.

#### ECONOMY: BETTER THAN NEIGHBORS, BUT ROOM FOR IMPROVEMENT

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¶15. Croatia's economy is the most developed of the former Yugoslavia, with the exception of Slovenia. Per capita GDP is approximately \$7,800, more than twice that of neighboring Serbia and Montenegro and roughly equal to Slovakia. Over the last six years, Croatia has enjoyed general macroeconomic stability characterized by low inflation and modest economic growth of approximately 4 percent annually. This growth, however, has been jobless, with the official unemployment rate remaining stubbornly high at approximately 18 percent.

¶16. The state still plays an overly large role in Croatia's economy. Although there has been progress in shedding some of the state's large portfolio of assets, notably banks, hotels and large agricultural combines, the government continues to be saddled with loss-making industrial companies whose subsidies drain approximately 3 percent of GDP annually. As a percentage of GDP, the state's role in the economy is far above the EU average at nearly 40 percent. With one pensioner for every 1.4 persons employed, above-average healthcare costs and out of control entitlement programs, the government faces many necessary, but politically unpopular decisions if it is to reduce chronic deficits and liberalize the country's economy.

¶17. Croatia missed out on the initial rush of foreign investment in Central and Eastern Europe following the fall of the Berlin Wall, largely because of the war in the former Yugoslavia, but also because of its slowness to make the difficult but necessary decisions to reform its economy. Foremost among the factors inhibiting greater investment is an inefficient judicial system that can take years to resolve even the most basic commercial disputes and a stubbornly Byzantine bureaucracy. There has been some improvement in this last area, with the government's creation of a "one-stop shop" for business registration and a trade and investment promotion agency to assist prospective foreign investors, but much more remains to be done.

¶18. Croatia is also saddled by large budget and trade deficits. Although the former has been reduced in recent years partially as a result of an IMF program, the latter has continued to balloon. Foreign debt, particularly in the private sector, has soared as well, now totaling over 80 percent of GDP. The fact that most of this debt is "euroized" limits Croatia's ability to let its currency depreciate, a large factor in its uncompetitive exports.

¶19. Croatia's political elite is fully cognizant of the need to further reform the economy and has made some recent progress in that direction, but much remains to be done to create the conditions to compete successfully in today's global economy. The beginning of EU accession negotiations has added new urgency to this fact.

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